The view from the city

Towards the top of every economic cycle, ‘red flags’ emerge that indicate an increasingly tenuous grasp between economic reality and inflated asset prices. In short, the net present value of money diminishes and future growing assets suddenly command stratospheric prices, based on highly optimistic expectations of future growth. This gap between value and growth is the eternal push/pull between present (cheap) value and future (expensive) growth. Until, that is, the spectre of rising inflation leads to a rotation from growth to value, where a bird in the bush is worth two in the hand.

Legal settlements are made for sums that seem beyond the dreams of avarice. For example, a Spanish court awarded former UBS banker Andrea Orcel €68m compensation for Santander reneging on an offer to become its next chief executive, while $105m was clawed back from Steve Easterbrook, the former CEO of McDonald’s, for his failure to disclose the breaking of internal company rules on resignation.

Princess Haya of Jordan, meanwhile, received a £554m divorce settlement from her former husband, the ruler of Dubai. These big-ticket settlements endorse the mood in the public mind of limitless financial assets and a diminishing grasp of reality.

In the background, there are often wild gyrations in markets, from cryptocurrency to developing market currencies. For example, cryptocurrencies such as Bitcoin and Ethereum halved in December 2021, with a total of $1.3tn – or 6% of US economic output – vaporised, while emerging market currencies such as the Turkish lira (TRY) hit a low of TRY18.4/$1, a huge depreciation from the average of TRY7.0/$1 in 2020.

Meanwhile, Jim Anderson, a fêted investment manager who oversaw the greatest transfer of value in history from traditional businesses to the FAANGs, chose to leave the party early and retire from Baillie Gifford and the Scottish Mortgage Trust. Similarly, respected retail industry veterans such as Terry Leahy and Tom Hunter, early backers of The Hut Group, took their money off the table on its IPO, despite the company being marketed as the future of e-commerce.

The resounding message here is “it’s as good as it gets”. That’s if anyone is listening while the party is in full swing.

The man on the Clapham omnibus has only just arrived at the party and he’s determined to have a great time. Conveniently, along comes Robinhood with its ‘meme stocks’ and an IPO in July 2021 at $38 per share, which peaked at $85 in August and collapsed to $12 by January. With lots of free money from furlough payments and lots of free time from WFH, every betting man starts punting the market. After all, with lockdowns, the usual gambling and sporting events, from footie to horse racing and the dogs, have been absent. These new retail punters gravitate towards the go-go growth stocks and so-called Covid beneficiaries, those online businesses – such as Zoom for work, Peleton for workouts, Ocado for groceries and Netflix for entertainment – dominating in lockdown.

Inevitably, as the ugly spectre of inflation raises its head, The Fed and Bank of England start to pull away the punch bowl and, overnight, these stocks became Covid-casualties, with faltering share prices.

> **“Big-ticket settlements endorse the mood in the public mind of limitless financial assets and a diminishing grasp of reality”**

In response to the pandemic, The Fed provided a wall of liquidity to incentivise risk-taking behaviour in the markets. Ark Innovation ETF, the flagship fund of disruptive new technologies cheerleader Cathie Wood, skyrocketed more than 150% in 2020, vying with Elon Musk’s SpaceX on a journey to Mars before duly collapsing to Earth last year.

Frenzied stock market activity is a sure sign of turbulent times ahead. The frenetic buying in late November 2021, with NASDAQ hitting daily record highs, was followed by furious volatility in late January. Wild market gyrations occur when there’s a crisis afoot, as in the run-up to the 2008 financial crisis. To underscore the impending doom, financial results in early February caused ructions among the FAANGs: Meta recorded a $200bn loss in market capitalisation, the biggest in stock market history, while, in contrast, Amazon recorded the biggest gain of $250bn. The FAANGs have grown to represent 25% of the US market, yet Meta’s share price collapsed by 20% like a penny stock. A cautionary tale of untrammelled greed and unrestrained capitalism coming home to roost.